

STATE OF MICHIGAN
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of)	
CONSUMERS ENERGY COMPANY for)	
the reconciliation of power supply cost)	Case No. U-17678-R
recovery costs and revenues for)	
the calendar year 2015.)	
_____)	

At the February 5, 2018 meeting of the Michigan Public Service Commission in Lansing,
Michigan.

PRESENT: Hon. Sally A. Talberg, Chairman
Hon. Norman J. Saari, Commissioner
Hon. Rachael A. Eubanks, Commissioner

ORDER

Procedural History

On March 31, 2016, Consumers Energy Company (Consumers) filed an application, with supporting testimony and exhibits, requesting approval of its reconciliation of power supply cost recovery (PSCR) expenses and revenues for the calendar year 2015, pursuant to 1982 PA 304 (Act 304), MCL 460.6j. Consumers' 2015 PSCR plan was approved in the June 9, 2016 order in Case No. U-17678 (June 9 order). On April 22, 2016, Consumers filed supplemental testimony and exhibits to reflect an adjustment to its transfer cost calculation and corresponding overrecovery calculation.

A prehearing conference was held on June 6, 2016, before Administrative Law Judge Sharon L. Feldman (ALJ). The ALJ granted petitions for leave to intervene filed by the Michigan

Department of the Attorney General (Attorney General); Midland Cogeneration Venture Limited Partnership (MCV); the Michigan Environmental Council and the Sierra Club, (jointly, MEC/SC); and the following biomass merchant plants (BMPs) collectively, Cadillac Renewable Energy, LLC, Genesee Power Station Limited Partnership, Grayling Generating Station Limited Partnership, Hillman Power Company, LLC, TES Filer City Station Limited Partnership (TES Filer City), Viking Energy of Lincoln, Inc., and Viking Energy of McBain, Inc. The Commission Staff (Staff) also participated in the proceeding.

An evidentiary hearing took place on April 20 and 21, 2017, at which, four witnesses testified and were cross-examined. The testimony and exhibits of the remaining 20 witnesses were bound into the record by agreement of the parties. On May 31, 2017, Consumers, the Staff, the Attorney General, MEC/SC, and the BMPs filed initial briefs. On July 11, 2017, reply briefs were filed by Consumers, the Staff, the Attorney General, MEC/SC, and the BMPs.

On November 17, 2017, the ALJ issued her proposal for decision (PFD). On December 11, 2017, exceptions were filed by Consumers, MEC/SC, and the Staff. Replies were filed by the BMPs, Consumers, MEC/SC, and the Attorney General. The record consists of 698 pages of transcript and 128 exhibits with portions of the evidentiary record and briefings marked confidential under the terms of the ALJ's September 9, 2016 protective order.

Positions of the Parties¹

Consumers

Stanley Hunley, a Principal Financial Analyst in the company's Electric Revenue and Fuel Reconciliation Section of the General Accounting Department, testified that the PSCR revenues collected from customers in 2015 totaled \$1,872,035,703. Exhibit A-5; 2 Tr 203. Mr. Hunley

¹ The ALJ provides a thorough overview of the record on pp. 3-28 of the PFD.

further provided that the company's 2015 PSCR expenses include fuel and purchased power costs, transmission costs, urea and aqueous ammonia costs, net nitrogen oxide (NO_x) and sulfur dioxide (SO₂) allowance costs, and transfer costs associated with renewable energy, less the cost of non-PSCR sales. 2 Tr 204-205. Mr. Hunley also explained that the company is requesting approval for lime costs in this and future PSCR cases. *Id.* Consumers explained that, as detailed by the testimony of several witnesses, the company's total expenses allocated towards the 2015 PSCR is \$1,867,498,397. Consumers' brief, p. 5.

In supplemental direct testimony, Mr. Hunley presented evidence showing a 2015 net PSCR overrecovery of \$9,916,771, inclusive of interest. Exhibits A-5 (supplemental), A-6 (supplemental); 2 Tr 205-209. In rebuttal testimony, Mr. Hunley explained that, based on testimony from the Staff and the BMPs, Consumers adjusted its net overrecovery for 2015, including interest, to \$12,184,568. Exhibits A-28, A-29; 2 Tr 216. Of the total net overrecovery, Mr. Hunley testified that \$4,773,521 results from rolling in the 2014 PSCR overrecovery, as provided by the Staff's calculations in Case No. U-17317-R. Exhibit S-1; 2 Tr 208.

The Staff

The Staff presented evidence showing that Consumers had a net 2015 PSCR overrecovery of \$19,753,728. Gretchen M. Wagner, an Auditor in the Commission's Act 304 Reconciliation Section of the Regulated Energy Division, explained the five adjustments she made to Consumers' initial filing.

Ms. Wagner first made a \$50,010 increase to Consumers' beginning balance to reflect the July 22, 2016 order in Case No. U-17317-R (July 22 order). 3 Tr 677. Ms. Wagner's second adjustment reflected a \$3,380,971 decrease to fuel for generation costs. *Id.* Ms. Wagner testified that the adjustment represents the removal of the total litigation costs of the company's complaint

against CSX Transportation (CSXT). Ms. Wagner further testified that the October 11, 2016 order in Case No. U-17918 (October 11 order) determined that the costs associated with the CSXT litigation were not costs appropriately considered in a PSCR proceeding.

Ms. Wagner's third adjustment reflected a \$7,155,965 disallowance of purchased power costs. Ms. Wagner's adjustment resulted from the testimony of Jill M. Rusnak² and Raushawn D. Bodiford.³

Fourth, Ms. Wagner made an adjustment to the August and November 2015 interest rates. Ms. Wagner testified that, due to the second and third adjustments above, the average underrecoveries shifted to overrecoveries. Thus, the company's August and November interest rates shifted from the short-term rate to the approved annual rate of return on equity of 10.3%.

Ms. Wagner's final adjustment was a \$1,197,742 increase to the total purchased and interchange power costs to reflect the difference between the amount requested for recovery by the BMPs and the amount the utility booked for 2015 BMP costs.

Mr. Bodiford also testified to an additional adjustment to reflect a proposed disallowance for the unplanned forced outage that occurred at the Campbell Unit 2 plant on October 19, 2015.

3 Tr 694.

The Attorney General

The Attorney General offered the testimony of Sebastian Coppola, an Independent Energy Business Consultant and President of Corporate Analytics, Inc., to support four recommendations related to Consumers' PSCR reconciliation. 3 Tr 641-669. The Attorney General first

² At the time of her testimony, Ms. Rusnak was a Public Utilities Engineer in the Act 304 and Sales Forecasting Section of the Commission's Regulated Energy Division.

³ Mr. Bodiford is a Public Utilities Engineer in the Act 304 and Sales Forecasting Section of the Commission's Regulated Energy Division.

recommended that the Commission disallow \$3,380,971 of litigation costs associated with the CSXT complaint. The Attorney General also pointed to the Commission's October 11 order to support his position that this expense is not properly included in a PSCR proceeding.

The Attorney General also recommended disallowance of \$6,315,809 in power purchase costs attributable to outages at Consumers' D.E. Karn (Karn) 1 and 2 generating units. Mr. Coppola testified that five outage incidents were due to incorrect design and installation of turbine rotor blades by a contractor hired by and under the supervision of Consumers. 3 Tr. 647.

Third, the Attorney General recommended that the Commission exclude \$1,507,249 of interest costs for years 2008 to 2014 related to an accounting error and recalculation of power purchase payments. The Attorney General argued that, although the principal amount owed would have been paid out to the BMPs had the accounting error not occurred, the interest payments are solely the result of the accounting error and should not be recovered in this PSCR reconciliation proceeding.

Finally, the Attorney General recommended that the starting balance for the 2015 PSCR balance be increased by \$50,010 to correctly reflect the Commission's July 22 order.

Michigan Environmental Council/Sierra Club

MEC/SC witness James Clift, the Policy Director for MEC, testified that the litigation costs for the CSXT litigation are not recoverable PSCR expenses. 3 Tr 600. MEC/Sierra also offered the testimony of George W. Evans, President of Evans Power Consulting, Inc. Mr. Evans testified that, in regards to coal purchases, Consumers relied on an unreasonably high energy price forecast. 3 Tr 609. Consumers' reliance, according to Mr. Evans, resulted in the company forecasting excessive operation of its coal-fired generating units, which ultimately resulted in excessive

purchases of contract coal for 2015. *Id.* Mr. Evans testified that Consumers use of the inflated forecast ultimately led to excess coal procurement expenses of \$1,995,583. 3 Tr 617.

Mr. Evans further testified that Consumers also entered into a costly coal supply contract that increased PSCR expenses by \$4,326,689. 3 Tr 609. Mr. Evans testified that the contract in question, labeled Contract No. 172, was unnecessary and resulted in increased purchases of contract coal by 436,049 tons over volumes indicated in the company's 2015 PSCR plan. *Id.*

Finally, Mr. Evans testified that Consumers did not take coal generating units off line when it would have been economical to do so. 3 Tr 621. Mr. Evans testified that Consumers also failed to leave units off line following an outage when it would have been economical to delay their return to service. *Id.* In further testimony, Mr. Evans calculated that the uneconomical operation of coal units drove up PSCR costs by \$8,791,554 in 2015. *Id.*

The Biomass Merchant Plants

The BMPs presented testimony addressing the following three issues: (1) the recovery of fuel and variable operation and maintenance (O&M) costs under 2008 PA 286 (Act 286), which costs are subject to a statutory cap under Act 286; (2) the Consumer Price Index (CPI) adjustment to the statutory cap; and (3) TES Filer City's recovery of certain environmental costs which are not capped under Act 286.

Proposal for Decision

The ALJ first determined that there were no remaining disputes on several key matters. First, the ALJ found no further dispute on the BMPs' request to recover \$13,197,742 in capped payments pursuant to MCL 460.6a(10), or payments of \$82,125 to TES Filer City for allowable expenses not subject to the cap. The ALJ further acknowledged Consumers' withdrawal of its request to recover \$3,380,971 in CSXT litigation costs in this proceeding. The ALJ further

recognized Consumers' adoption of the increase of \$50,010 to the beginning 2015 PSCR reconciliation balance based on the July 22 order, and a \$2,808 adjustment to reflect replacement power costs for the Campbell Unit 2 outage as recommended by Mr. Bodiford.

The ALJ determined that the following four issues remained in dispute: (1) whether Consumers is responsible for the replacement cost of power associated with certain outages at the Karn 1 and 2; (2) whether any disallowances are warranted for Consumers' operation of its coal-fired generating units; (3) whether any disallowances are warranted due to Consumers' over-projection of its coal requirements; and (4) whether the Commission should exclude interest costs associated with the revised power purchase agreement (PPA) payments for 2008-2014. PFD, p. 29.

Discussion

Karn Outages

The underlying facts related to certain outages at the Karn 1 and 2 remain largely undisputed. After one of the low-pressure (LP) turbine rotors failed in 2008, Consumers determined that the remaining LP rotors at Karn 1 and 2 were reaching their end of life and began taking steps for replacement. 3 Tr 576. After conducting a structured bid evaluation process, Consumers contracted with Alstom Power Inc. (Alstom) to replace the rotors. 3 Tr 565. Alstom was selected based on its design, cost to perform work, and its reputation of having the highest success rates in the industry. *Id.* Alstom completed the initial replacement of the turbines in December of 2014. 3 Tr 685. According to the Staff, a design error in the initial Alstom work required Consumers to order the turbines to be replaced again just 11 days after the completion of the first replacement project. *Id.*

Both the Staff and the Attorney General recommended disallowance of replacement power costs during a series of outages at Karn 1 and 2 in 2015. The Staff argued that Consumers should be responsible for the outages during the second replacement period arising from the design flaw. Staff's brief, p. 6. The Staff averred that Consumers was in the position to properly supervise the work of Alstom, questioned the contractor about problematic clearances, and ultimately approved the design. *Id.* The Staff claimed that it was Consumers, not PSCR customers, that was in a position to follow through with design questions in Alstom's initial work and it would be inequitable to require PSCR customers to pay for the associated costs when they already paid for replacement power costs during the initial turbine work. *Id.*

To support the Staff's proposed disallowance for replacement power purchases, Ms. Rusnak testified that a series of outages at Karn 2 from January 1, 2015, to May 17, 2015, were directly attributable to the initial 2014 turbine replacement. The total replacement power purchases, and recommended disallowance, for the 132 outage days at Karn 2 is \$5,626,997. *See*, Exhibit S-9.

Ms. Rusnak also testified that outages at Karn 1 from February 26, 2015, through March 2, 2015, and April 24, 2015 through June 14, 2015, were directly attributable to the design issue. 3 Tr 688-689. The Staff argued that the replacement power purchase cost for these outages totaled \$1,528,968 and should be disallowed. Staff's initial brief, p. 7.

The Attorney General also claimed that replacement power purchase expenses for outages caused by the design flaw should be disallowed and for the same reason advocated by the Staff. The Attorney General's witness, Mr. Coppola, testified that the design error directly attributed to the combined outages at Karn 1 and 2. 3 Tr 651. The Attorney General's calculations for replacement power purchases resulting from these outages and recommended disallowance is \$6,315,809. The Attorney General further argued that Consumers should retain the \$1.5 million in

insurance proceeds flowing from the design error and therefore should not be deducted from the disallowance. MEC/ Sierra Club agreed with the Attorney General's position.

Consumers argued against any disallowance for the design error and against disallowance for replacement power costs for several of the outages from Ms. Rusnak's aggregated calculation for Karn 2. First, Consumers contended that it could not be held liable for any replacement power purchase costs related to the 2015 turbine repair work, because the company could not examine the proprietary design of Alstom and reasonably relied on Alstom's reputation in the industry and its success in completing similar work at Talen Energy's Brunner Island Power Plant. Consumers also pointed to the record evidence of David B. Kehoe, Executive Director in the Energy Resources Business Services unit, when he testified that:

During the build package review, Consumers Energy reviewed and questioned Alstom's change in clearances, as Alstom's clearances were different from the original equipment manufacturer's clearances. Alstom indicated that the details of its new retrofit design were intellectual property and therefore confidential to the customer. However, Alstom did explain that the performance improvements are achieved through tighter clearances and the additional stage of blades (used to gain MWs) closes up these clearances. Based on its expertise and experience, Alstom was confident in its design and clearances. Furthermore, the [c]ompany believed that it was reasonable to rely on Alstom's recommendation based on Alstom's recent, and successful, experience completing similar work.

3 Tr 565. Consumers argued that its reliance on Alstom's expertise in turbine replacement and Alstom's opinion regarding the clearances does not establish Consumers' negligence or that Consumers unreasonably or imprudently managed the Alstom's turbine replacement work. Consumers' reply brief, p. 7.

Consumers further argued that certain outages at Karn 2 aggregated by the Staff in its calculation of the disallowance are not properly included in the 2015 PSCR reconciliation. Consumers agreed the company incurred \$6,315,805 in replacement power costs for both Karn 1 and 2, but the additional \$840,160 disallowance proposed by the Staff resulted from

other events. Consumers' reply brief, p. 10. More specifically, Consumers pointed out that Mr. Kehoe testified that the periodic outage report for that time period, which was provided to the Staff, indicated that the final root causes for these outages was from "Chemical Cleaning from Boiler" and "Condensation forming in Reheat ('RH') inlet pendants." *Id.*, quoting 3 Tr 560.

The ALJ disagreed with Consumers' argument regarding the aggregated outages and stated:

For Karn 2, this PFD finds that Staff correctly concluded that the series of outages in 2015 at Karn 2 from January 1 through May 17, 2015, were related to the design flaw. Consumers Energy acknowledged that Staff did not rely only on the information presented in the company's Exhibits A-8 and A-10, but conducted a more thorough inquiry. A review of the information available on this record support's Staff's conclusion that the work done on the unit during January, prior to the January 31 start of the major 104-day outage, was at least in part an effort to address the vibrations the unit was experiencing, that we now know were due to the rubbing caused by the differential expansion. A review of Ms. Rusnak's Exhibit S-7, also Exhibit A-32, shows that other repair activities taking place at the unit occurred within the context of an unacceptable level of vibrations. While the unit ran for approximately 4 days in January (January 15-19) before the January 31 shutdown, Consumers Energy did not establish that the unit could have been run for any period longer than the few days it did run given the rubbing that was taking place and the damage that was occurring. As Ms. Rusnak testified, the unit ran only approximately 11 days total following the 2014 turbine installation. Note that the root cause analysis concluded that the rubbing began with the first startup of the unit, and it reported that the unit would not start on January 31.

PFD, p. 44. The ALJ further found that the March 9, 2015 root cause analysis could not have been completed before the January 31, 2015 failed start up. The ALJ further found it hard to believe that Consumers could have effectively planned the work needed to be done to replace the LP turbine rotors in advance of that date, to constitute a "planned outage." The ALJ determined that even if that there was planned scope of work beginning on January 31, the damage to the rotors was only found after January 31, and the resulting outage should have been coded as a forced

outage. PFD, p. 46. There was no disagreement that the outages at Karn 1 were due to the initial turbine rotor replacement work.

The ALJ further determined that Consumers was responsible for all replacement power purchases as proposed by the Staff. The ALJ was not persuaded by Consumers' argument that the disallowances related to decision making in the prior PSCR year. The ALJ found that the disallowances related to only 2015 plant outages and that the underlying decisions could not have been effectively reviewed in the 2014 PSCR plan year, because Consumers was not required to report the 2015 outages in the 2014 PSCR reconciliation. PFD, p. 42. The ALJ noted that Act 304 directs the Commission to disallow replacement costs of power for outages over 90 days, unless the utility establishes that the outage was not caused or prolonged by the utility's negligence or by unreasonable or imprudent management. *Id.* The ALJ concluded that Consumers failed to meet this burden and was responsible for the replacement power purchases. PFD, p. 40. The ALJ stated that Consumers did not provide clear and satisfactory evidence that it undertook all reasonable steps to protect ratepayers once it learned that Alstom's design clearances were tighter than the original manufacturer's clearances. PFD, p. 41. Additionally, the ALJ found that Consumers did not establish that it was diligent in addressing its concerns regarding the clearances. *Id.* As a final measure, the ALJ reduced the disallowance to \$5,655,965 to reflect that Consumers eventually booked the \$1.5 million of insurance proceeds as a credit to PSCR costs. PFD, p. 46.

The Staff takes exception to this final measure taken by the ALJ. The Staff argues that the correct disallowance should be the total replacement cost of power of \$7,155,965, with any business interruption insurance proceeds accruing to the company. Staff's exceptions, p. 1. The Staff argues that past Commission practice is to offset proceeds only when replacement power

costs are included in PSCR expenses, and when the Commission disallows replacement power costs, then the insurance proceeds are not netted against the total replacement power cost disallowance. Staff's exceptions, p. 2.

Consumers takes exception to the ALJ's recommendation to hold the utility responsible for the replacement power purchases and for including in that recommendation the additional \$840,160 in unrelated Karn 2 expenses. Consumers again argues that it cannot be held responsible for the outages caused by the Alstom design flaw. Consumers continues to argue that Alstom's designs were intellectual property and that it is standard in the industry to keep the manufacturer's intellectual property confidential, especially from third parties. Consumers further argues that it provided prudent oversight and management of the project. Consumers avers that it questioned Alstom about the change in clearances and was ultimately satisfied that Alstom sufficiently explained the differences before the contractor proceeded with the repair work. Consumers' exceptions, pp. 5-6. Consumers reiterates that, although it did not examine the details of the proprietary design, it reasonably relied on the expertise of Alstom given that company's reputation in the industry. Consumers' exceptions, p. 6. Consumers also takes exception to the PFD's recommendation to include the additional \$840,160 in replacement power purchase from Karn 2 outages. Consumers argues that these costs were not linked to the LP turbine rotor replacement and should not have been aggregated. Consumers' exceptions, p. 11.

The Staff replies that the Commission should not allow Consumers to take refuge in Alstom's expertise and proprietary design. Staff's replies to exceptions, p. 3. The Staff further argues that Consumers must bear the responsibility for the decisions it makes, which includes allowing Alstom to deviate from the original manufacturer's clearances. *Id.* The Staff also replies that the ALJ properly aggregated the outages at Karn 2 because the utility did not present clear and

satisfactory evidence that the outages in question were not caused by the negligence or by unreasonable or imprudent management of the company.

The Commission agrees with the Staff and finds that the total disallowance for replacement power supply costs for outages at Karn units 1 and 2 following the LP turbine rotor replacement work performed by Alstom is \$7,155,965. The Commission further agrees that the total disallowance should not be offset by the business interruption proceeds Consumers received. Under Act 304, Consumers has the burden of proof to establish that its decisions were reasonable and prudent. In addition, MCL 460.6j(13)(c) specifically requires the Commission to:

Disallow net increased costs attributable to a generating plant outage of more than 90 days in duration unless the utility demonstrates by clear and satisfactory evidence that the outage, or any part of the outage, was not caused or prolonged by the utility's negligence or by unreasonable or imprudent management.

Despite its statutory obligation to demonstrate that its actions were reasonable and prudent, Consumers did not provide the requisite evidentiary record to support that the management decisions it made in overseeing the LP turbine rotor replacement project were reasonable and prudent. The Commission agrees with the Staff and the Attorney General that once the company understood that the clearances were different than those of the original equipment manufacturer, Consumers should have done more than merely rely on Alstom's reputation in the industry. This clearance deviation should have triggered Consumers to act more prudently to protect its PSCR customers from the replacement power costs incurred.

The Commission also adopts the ALJ's recommendation to accept the Staff's evidence connecting the 2014 LP turbine replacement outage to the 2015 outages Consumers experienced to repair the same work. *See*, Exhibits S-3 and S-6. The Commission finds that the aggregated 2015 outages resulted from the insufficient clearance issue, which was imprudently managed by Consumers.

Coal Unit Dispatch Decisions

MEC/SC argued that, because Consumers designated its coal units as must-run during extended periods where the units operated at a loss, the company ignored its own net energy value (NEV) forecast, and provided no legitimate reasons for forcing the uneconomic use of its coal-fired units, the Commission should disallow recovery of the resulting unnecessary PSCR expenses. MEC/SC's initial brief, p. 5.

MEC/SC contended that, in its 2015 PSCR plan case, Consumers claimed that it would consider market conditions in deciding whether to commit its coal units as must-run resources. *Id.*, p. 8. MEC/SC averred that the record evidence demonstrates that Consumers did not follow through with its claim. MEC/SC argued that for an extended period of time, Consumers failed to decommit its coal units even though the unit's costs were greater than the revenues received from Midcontinent Independent System Operator (MISO). MEC/SC asserted that Consumers incurred millions of dollars of unnecessary fuel costs by continuing to designate these units as must-run, rather than bringing them off-line when market conditions warranted that result. *Id.*

MEC/SC witness, Mr. Evans, identified various periods in 2015 that Consumers operated its coal-fired units uneconomically. 3 Tr 625-628. These periods included, as Mr. Evans testified, when the units were already operating and should have been taken off-line, and when Consumers could have delayed an off-line unit's return to operation. MEC/SC initial brief, p. 10. Mr. Evans offered Exhibit MEC-16 to demonstrate the instances where MEC/SC alleged Consumers coal units operated at a loss in 2015. Mr. Evans testified that Consumers could have saved \$4,134,240 in PSCR costs had the company delayed returning an off-line unit to operation. 3 Tr 626. Mr. Evans further testified that he calculated that Consumers incurred \$4,657,314 in unnecessary fuel costs by failing to decommit already running units during uneconomic periods. *Id.* MEC/SC

further argued that Consumers never used its own NEV forecasts in 2015 to consider taking an operating coal unit off-line and continued to designate those units as must-run at all times.

Mr. Evans explained that the NEV forecasts are prepared each day and compare the estimated cost of operating a generating unit in each hour of the upcoming 30 days to the estimated market revenues the company could expect to earn during the same time period. 3 Tr 631-632.

MEC/SC claimed that running a coal-fired unit as a must-run when it is uneconomical to do so requires the company to unnecessarily feed the plant with coal, burning fuel, and incurring PSCR costs. MEC/SC asserted that in calculating the savings during these periods of uneconomic use, Mr. Evans properly used “as burned” coal costs. MEC/SC initial brief, p. 20. MEC/SC further argued that using as-burned costs is appropriate because they are the actual coal costs charged to customers through the PSCR factor. *Id.*, p. 21. Thus, MEC/SC argued, as-burned coal costs are the only appropriate measure of ratepayer impact from Consumers’ operation of its coal units. *Id.*

Consumers contended that MEC/SC erroneously relies on as-burned cost of coal to determine economic dispatch of the coal-fired generating plants when replacement cost of coal should have been used. Consumers argued that the same erroneous position regarding as-burned coal has been presented and rejected in numerous PSCR proceedings. Consumers further argued that MEC/SC’s use of as-burned coal in this case completely skews the periods of purported uneconomic generating operations claimed by MEC/SC. Consumers further argued that the modeling done by Mr. Evans improperly relied on as-burned coal. Due to this improper use of the as-burned cost of coal, no portion of Mr. Evans’ analysis is salvageable.

Consumers also argued that MEC/SC misunderstands how the NEV forecast is used and is based on Mr. Evans’ flawed analysis that improperly identified periods of uneconomic use. Additionally, Consumers argued that the manner in which the coal-fired plants are offered as

must-run units has routinely been approved by the Commission. Consumers asserted that its coal-fired plants are baseload plants, have complex start-up and shut-down processes, and are offered in a manner in which they are designed to operate. Consumers further argued that even though the company typically does not cycle its coal-fired plants it does continuously evaluate the economics of its generating units to determine where savings could be realized by turning off a unit.

However, Consumers argued, turning off and on a coal-fired plant does not extract maximum efficiencies of the units. Consumers provided evidence that, when the NEV forecast indicates that a generating unit is likely to receive revenue in excess of the total cost of production over the period of interest, the company offers the unit as a must-run resource to ensure it is committed into the MISO market. 2 Tr 253. The company further provided that when the NEV forecast indicates that a generating unit is not likely to receive revenue in excess of the total cost of production plus start-up cost and a \$25,000 start-up adder over a period of interest, the units are offered as an economic resource. 2 Tr 254. In offering its units, Consumers argued, NEV forecasts are extremely helpful but the company also relies on its experience and expertise in offering generating units into the MISO market and that all factors known by the company at the time the offer is made must be considered.

None of the other parties weighed in on this issue.

The ALJ noted that the most significant item of disagreement between MEC/SC and Consumers in determining whether the company's units were operating at a loss is the appropriate coal cost to use in the NEV calculations. PFD, p. 52. The ALJ recommended that the replacement cost of coal be used in the analysis to determine if any of the units are operating at a loss. PFD, p. 53. The ALJ further provided that the use of the replacement cost of coal is consistent with the NEV projections that are used in the company's decision-making process. Additionally,

the ALJ noted that, in Case No. U-17317, Consumers' 2014 PSCR plan case, "the Commission endorsed the use of the replacement cost of coal in projecting the net energy value of operating a generating unit and in bidding the unit into the MISO market, rather than the as-burned cost of coal." *Id.*

The ALJ also rejected MEC/SC's argument that MCL 460.6j mandates that the as-burned cost of coal be used in the analysis. The ALJ stated:

Nothing in Act 304 prescribes a specific method for evaluating the reasonableness and prudence of utility decisions, and nothing prescribes a formula for determining an appropriate disallowance in the event a decision has been unreasonable or imprudent. MCL 460.6j(12) requires the Commission to "consider any issue regarding the reasonableness and prudence of expenses for which customers were charged if the issue was not considered adequately at a previously conducted power supply and cost review." MCL 460.6j(14) directs the Commission to "require an electric utility to refund to customers or credit customers' bills any net amount determined to have been recovered over the period covered in excess of the amounts determined to have been actually expensed by the utility for power supply, and to have been incurred through reasonable and prudent actions not precluded by the commission order in the power supply and cost review." Similarly, MCL 460.6j(15) requires the Commission to "authorize an electric utility to recover from customers any net amount by which the amount determined to have been recovered over the period covered was less than the amount determined to have been actually expensed by the utility for power supply, and to have been incurred through reasonable and prudent actions not precluded by the commission order in the power supply and cost review." While the Commission is not bound by any single formula in determining appropriate disallowances under these sections, the threshold question in this case is whether the utility's commitment decisions were reasonable and prudent, and it is fundamentally incompatible with the approved decision-making standard--the net economic value of a commitment decision based on the replacement cost of coal--to determine the reasonableness and prudence of a commitment decision based on the as-burned cost of coal. Act 304 does not foreclose using an opportunity-cost standard in determining the amount of a disallowance.

PFD, pp. 54-56. The ALJ reviewed Consumers' Exhibit A-24⁴ showing that the company's decision-making over the relevant time period resulted in a savings of approximately \$1.1 million.

⁴ The ALJ conducted a thorough review and analysis of Exhibit A-24 on pp. 56-68 of the PFD, which the Commission adopts in full.

PFD, p. 56. The ALJ rejected MEC/SC's calculations from Exhibit MEC-16 showing a total \$8.8 million loss, because the calculations used the as-burned cost of coal and are therefore not persuasive evidence supporting MEC/SC's argument regarding Consumers' uneconomic decision-making in offering its coal-fired plants. *Id.*

The ALJ did raise concern with some of Consumers' discovery responses, an issue raised by MEC/SC. One problematic area, the ALJ noted, involved the details of the NEV calculations. Although the ALJ did not recommend an adverse inference due to the poor-quality of some of Consumers' responses to discovery requests, the ALJ recommended that the Commission make clear that the company "may be held accountable in future cases for a failure to carefully and accurately respond to discovery responses, or for a failure to revise those discovery responses when the person who provided them realizes they are not accurate." PFD, p. 78.

Ultimately, the ALJ found that a disallowance was not recommended based on her evaluation of the economics of Consumers' operation of its coal-fired plants. PFD, p. 78. The ALJ found that the MEC/SC's evidence was unpersuasive due to its reliance on the as-burned cost of coal in its calculations. And although the ALJ found Consumers' Exhibit A-24 sufficiently reliable to support her recommendation, the lack of documentation of the company's decision-making was troubling. PFD, p.79. The ALJ recommended that in future cases, the Commission should articulate an expectation that Consumers will present a thorough analysis of its decision making-process in future applications, and will retain documentation of that process. PFD, p. 80.

Consumers takes exception to the PFD, but only to address the ALJ's recommendation that the Commission should consider addressing the extent to which the company is expected to retain documentation of its decision-making process in offering its generating units. Consumers points

out that it provided extensive amounts of information related to its decision-making process, which included documentation of the company's generating offers on a daily basis.

MEC/SC takes exception to the ALJ's recommendations that the Commission find that:

(1) Consumers operated its coal-fired generating units economically; and (2) evaluation of Consumers' coal-fired generating unit dispatch decisions on the basis of replacement coal costs is reasonable. In regards to the economical operation of Consumers coal-fired generating units, MEC/SC reargues the positions that it offered in briefing. The ALJ thoroughly explained her recommendations regarding each decision questioned by MEC/SC on pages 56-68 of the PFD, which the Commission adopts in full.

The Commission's previous orders have clearly stated that evaluating the company's decisions to offer its coal-fired plants using the replacement cost of coal is reasonable. In Case No. U-17317, the Commission stated:

In the modeling used to forecast the dispatch of its plants, and in actual bidding, Consumers uses the "replacement" cost of coal, *i.e.*, the spot-market price of coal, rather than the cost of coal in the company's inventory, *i.e.*, the "as-burned" cost. According to MEC/SC, bidding based on spot market coal, which is often less expensive than contract coal, provides erroneous modeling outcomes and may result in the uneconomical dispatch of the company's coal plants. Consumers responded that the Commission has repeatedly affirmed Consumers' use of replacement coal costs in determining the reasonableness of its dispatch modeling. Consumers adds that its methodology conforms to industry standards and that, because the majority of the company's coal is under contract (*i.e.*, a fixed cost), the only cost to be factored into the dispatch determination is the variable cost of replacement coal.

Commission's May 20, 2016 order in Case No. U-17317, p. 10. The Commission then determined:

[a]lthough MEC/SC presented some new arguments on this issue, their presentation was insufficient to overcome the fact that using as-burned coal costs in modeling and bidding the company's units would necessitate bidding on the basis of sunk costs, rather than variable costs, thus violating principles of economic dispatch and MISO rules. In addition, as Consumers pointed out, the Commission has previously found that MEC/SC's recommendation is not standard in the industry and could introduce additional risks that could ultimately result in higher customer costs.

Id., at p. 15. Additionally, in its June 9, 2016, the underlying plan case for this reconciliation, the Commission reaffirmed the above decision. Thus, as the ALJ pointed out, the Commission has previously determined that it is reasonable and appropriate for Consumers to use the replacement cost of coal, rather than the as-burned cost of coal, in making its commitment decisions for the generating units.

The Commission therefore agrees with the ALJ and rejects MEC/SC's request for disallowances related to Consumers' economic evaluations in the operation of its coal-fired generating units. The Commission finds that MEC/SC's arguments are misplaced because of its continued reliance on the cost of as-burned coal when evaluating Consumers' decisions.

In regards to the discovery issues and more thorough documentation of its decision-making addressed by the ALJ, the Commission points out that Consumers should be well aware of evidentiary burden under Act 304 and the duty of the Commission to disallow expenses when that burden is not satisfied.

Coal Purchases

MEC/SC argued that the Commission should disallow approximately \$2 million related to Consumers coal procurement in 2015 because the company failed to adhere to spot coal purchases in its 2015 PSCR plan, or alternatively, to disallow approximately \$4.3 million as a result of the company entering into Contract 172. MEC/SC's initial brief, p. 55. MEC/SC first argued that Consumers' coal procurement decisions unreasonably favored higher-priced contract coal over lower-priced spot market coal. *Id.*, p. 45. MEC/SC argued that the Mercury and Air Toxic Standards (MATS) adder resulted in an inflated projection of coal requirements and therefore resulted in a shift in the proportion of contract coal to spot market coal. *Id.*, pp. 45-46. MEC argued that had Consumers used the correct proportion of contract coal to spot market coal, the

savings to PSCR customers would have been \$1,995,583. *Id.* at p. 46. MEC argued that the company should have performed a revised PROMOD IV run to demonstrate the impact of removing the MATS adder. *Id.*, p. 44.

Consumers argued that it should not be held to a precise portfolio of contract and spot purchases because it would preclude the company from exercising flexibility in its purchasing decisions. In support of allowing flexibility in its purchasing decisions, Consumers witness Stephen J. Nadeau, a Senior Fuel Procurement Analyst in the Fossil Fuel Supply Department, testified that:

The [c]ompany's strategy for coal procurement provides for purchasing and securing quantities of coal over time that typically enable the [c]ompany to have approximately 70% to 90% of its anticipated volume requirements secured by the fall of each year for the following calendar year. The [c]ompany employs this strategy because the spot coal market by its nature can be unpredictable and can easily become constrained by forces affecting both supply and demand. Accordingly, the [c]ompany believes it is best to manage its coal supply in a manner such that the risk of having an insufficient supply of coal is minimized while at the same time balancing pricing considerations by retaining some exposure to the spot market. To manage this risk, the [c]ompany limits its exposure to the spot market by contracting for a large percentage of its projected requirements ahead of time because it does not believe it is reasonable or prudent to speculate that large quantities of coal will be available when needed from the spot market. Furthermore, this strategy provides coal supply protection should the [c]ompany's actual coal requirements change from its projected requirements.

3 Tr 441.

Consumers also argued that the evidence in this case reveals that a MATS adder did not result in an inflated projection of the company's coal requirements. Consumers' replies to exceptions, p. 51. Consumers also disagreed with MEC/SC's position to run a revised PROMOD IV run. According to Consumers, the evidence it presented definitively demonstrated that the incremental cost of production used to dispatch the company's coal-fired units are well below the energy market prices used to dispatch the same resources, with or without the MATS adder. *Id.*, p. 58.

Consumers argued that the lower production from the company's coal-fired units in 2015 was not due to the use of the MATS adder, but resulted from lower-than-expected energy market prices.

Id. Consumers contended that MEC/SC's arguments merely assume that the MATS adder accounted for a significant portion of the variance between PSCR plan and actual locational marginal pricing (LMP). *Id.*, p. 59. However, Consumers argued, MEC/SC failed to take into account, and failed to quantify, the extent to which the company's percentage of contract coal would have increased absent the MATS adder. *Id.*

The ALJ first determined that Consumers failed to run a revised PROMOD IV analysis to show the coal requirements it would have projected without the MATS adder. PFD, p. 87. Therefore, the ALJ continued, Consumers has not established that the use of the MATS adder could not have resulted in a material overprojection of coal-fuel generation in 2015. *Id.* The ALJ, however, could not conclude from the record evidence that an overprojection would cause increased cost to PSCR customers. *Id.*

The ALJ also reviewed Contract 172 and found that although the per-million British thermal units (MMBtu) price is above the average spot market price, it is below one of the spot market purchases made in 2015. *Id.* The ALJ also reviewed Contracts 167, 169, and 176 and found no material issues related to the 2015 PSCR reconciliation. The ALJ also found persuasive Mr. Nadeau's testimony that Contract 172 was the product of competitive bidding, and was 5% below market price at the time. *Id.*; *see also* 3 Tr 453. When reviewing the totality of the circumstances and the evidence presented, the ALJ could not recommend the disallowance proposed by MEC/SC. PFD, p. 89.

MEC/SC takes exception to the PFD on several grounds. The Commission, however, finds that the exceptions merely echo the arguments MEC/SC previously made in its initial and reply

briefs. The Commission further finds that the ALJ's recommendations are well-reasoned and should be adopted. As the ALJ noted, the record evidence does not demonstrate that an overprojection of coal-fueled generation would have resulted in higher prices to the PSCR customer. Thus, for purposes of the 2015 PSCR reconciliation, it is immaterial that Consumers failed to run the PROMOD IV analysis without the MATS adder. The Commission also agrees with the ALJ's findings regarding Contract 172. As the ALJ noted, the contract was competitively bid, was 5% below the market price at the time, and the per-MMBtu price was below one of Consumers spot market purchases made in 2015.

Interest on the Power Purchase Agreements Payments

In 2015, Consumers made additional payments under various power purchase agreements (PPAs) to rectify underpayments in years 2008-2014, which affected the net calculation of the energy charges for the period of April 1, 2009 through May 2015. 2 Tr. 227. Provisions of some of the PPAs required that interest be included in the repayment. *Id.* The interest payments totaled \$1,507,249. *Id.*

The Attorney General argued that Consumers should be responsible for the error, and the Commission should disallow recovery of this amount. Attorney General's initial brief, p. 13. The Attorney General further argued that the additional interest reimbursements should not be passed on to ratepayers. *Id.*

The ALJ agreed with the Attorney General and recommended that the Commission disallow the interest expense. PFD, p. 93. The ALJ determined that Consumers did not adequately explain why the accounting error occurred. *Id.* The ALJ further provided that MCL 460.6j requires that PSCR costs approved for recovery be incurred through reasonable and prudent actions. The ALJ

stated that the record evidence does not establish that the interest payments were reasonably and prudently incurred. *Id.*

Both Consumers and the BMPs take exception to the PFD. Both parties argue that the interest payments are a contractual component of the PPAs that were approved by the Commission. Because the principal amount would have been paid to the power suppliers and recoverable during the respective PSCR years, Consumers and the BMPs argue, the interest is directly attributable to the PSCR expense because the interest provisions are incorporated into the PPAs and are recoverable PSCR expenses.

The Commission disagrees with Consumers and the BMPs. As the ALJ noted, Act 304 requires Consumers to demonstrate that expenses are incurred through reasonable and prudent actions before the Commission may approve recovery. Consumers did not meet its burden regarding this expense and thus the Commission finds that the expense is disallowed.

The Staff's Exception 2

As a final matter, the Commission agrees with the Staff's exception to the PFD regarding the omission of the \$82,125 in Cross State Air Pollution Rule (CSAPR) allowance costs that were incurred in 2015. The ALJ accepted TES filer's position regarding this CSAPR expenses and it should be included in the overrecovery calculation. The Staff argues that when adjusting for the CSAPR expense plus interest yields a corrected overrecovery of \$19,671,250. In addition, when accounting for the PPA interest disallowance, the total overrecovery is \$21,178,499.

THEREFORE, IT IS ORDERED that:

A. The application for a power supply cost recovery reconciliation for calendar year 2015 filed by Consumers Energy Company is approved, as modified by this order.

B. Consumers Energy Company's net overrecovery balance of \$21,178,499, inclusive of interest, shall be reflected as the company's 2016 power supply cost recovery reconciliation beginning balance.

The Commission reserves jurisdiction and may issue further orders as necessary.

Any person desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order, pursuant to MCL 462.26. To comply with the Michigan Rules of Court's requirement to notify the Commission of an appeal, appellants shall send required notices to both the Commission's Executive Secretary and to the Commission's Legal Counsel. Electronic notifications should be sent to the Executive Secretary at mpscedockets@michigan.gov and to the Michigan Department of the Attorney General - Public Service Division at pungpl@michigan.gov. In lieu of electronic submissions, paper copies of such notifications may be sent to the Executive Secretary and the Attorney General - Public Service Division at 7109 W. Saginaw Hwy., Lansing, MI 48917.

MICHIGAN PUBLIC SERVICE COMMISSION

Sally A. Talberg, Chairman

By its action of February 5, 2018.

Norman J. Saari, Commissioner

Kavita Kale, Executive Secretary

Rachael A. Eubanks, Commissioner